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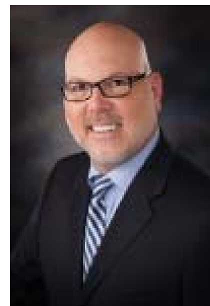
DOL Will not Enforce Its New Fiduciary Regulation Pending Review After Federal Appeals Court Strikes the Rule Down

By Anthony L. Scialabba, Esq.

On March 16, 2018, the Department of Labor ("DOL") announced that it would not enforce its new fiduciary regulation "pending further review". A DOL spokesman provided no additional details in this regard.

The government's decision came one day after the U.S. Court of Appeals in the 5th Circuit struck down the regulation. In a two to one vote, a three-judge panel in in the 5th Circuit reversed a pro-regulation ruling issued by a U.S. District Court judge in Dallas in February 2017 that dismissed legal challenges to the rule by several organizations including the U.S. Chamber of Commerce. In writing the majority opinion, Circuit Court Judge Edith Jones stated: "When agencies within the executive branch defy

Brian McCabe joins RetireWell Administrators, Inc.



RetireWell Administrators, Inc. is pleased to announce that Brian McCabe joined the firm as a Partner and Vice President of Operations and Sales. Brian's responsibilities include the day-to-day management of the Operations team as well as leading the sales and marketing effort of RetireWell through the establishment and maintenance of relationships with our many different partners in the retirement plan community.

"Brian's hire demonstrates RetireWell's commitment to providing best-in-class service to our clients and partners as well as a commitment to growth. Brian is an excellent addition to

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congressional limits, they lord it over the people without proper authority….". She added that he fiduciary rule is unreasonable based on legal precedent, and it represents "arbitrary and capricious exercises of power….".

The Court of Appeals ruling and the DOL response has caused uncertainty within the retirement and financial services industries. It remains to be seen as to whether the U.S. Supreme Court, U.S. Congress, the Securities and Exchange Commission or the states will attempt to resolve this matter.

Brian McCabe joins RetireWell Administrators, Inc...cont'd

our management team whose experience and leadership is highly valued.” ***Anthony L. Scialabba, Esq. President and CEO***

Brian has over 20 years of experience in the financial services industry from some very well-respected firms including T. Rowe Price, United Retirement Plan Consultants and Nova 401(k) Associates. He is a graduate of Western Maryland College with a Bachelor of Arts degree in Business Administration and Economics. He is an active member of the American Society of Pension Professionals & Actuaries (ASPPA) and holds both the Qualified Pension Administrator (QPA) and Qualified 401(k) Administrator (QKA) designations. In addition, Brian is certified as an Accredited Investment Fiduciary® (AIF®). His consultative approach, commitment to best-in-class service and his in-depth knowledge of the industry builds, maintains and grows long- lasting client and partner relationships.

“I have known Brian for the better part of 23 years and have worked with him professionally since 2003. Without a doubt, Brian is a consummate professional. The service model he follows is second to none and he is constantly on top of industry changes. I hold his ability, integrity and service in the highest regard and all of my clients have benefited from having Brian as their advocate in the Retirement Planning aspects to their business.” ***Steven A. West, Financial Advisor, Bethesda, MD***

Brian resides in Perkiomenville, Pennsylvania. He enjoys spending time with his two children, travelling, golfing, enjoying a unique beer and being a fan of the Super Bowl champion Philadelphia Eagles.

Congress Changes Rules Concerning Hardship Distributions

By Anthony L. Scialabba, Esq.

Recently this year, as a part of the Bipartisan Budget Act of 2018, three key changes were made to the retirement plan "hardship withdrawal" rules. These changes are effective with respect to plan years beginning after December 31, 2018. The following discusses these new rules.

First, one of the modifications made by the Act concerns hardship distributions and “earnings on deferrals”. Prior to the Act, a participant could receive earnings on employer matching contributions and employer nonelective contributions, but not on elective deferral contributions. Congress recognized that there was no reason for this disparate treatment. Thus, the new law resolves this issue by aligning the treatment of earnings on elective deferral contributions with the way employer matching and employer nonelective contributions are treated. Thus, the Act provides that hardship withdrawals may be taken from earnings on deferrals. The Act also permits hardship withdrawals to be taken from earnings on Qualified Nonelective Employer Contributions, Qualified Matching Contributions and safe harbor sources.

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Second, to receive a distribution on account of incurring a "hardship", a participant must have a heavy and immediate financial need. In addition, he or she can only receive an amount that is necessary to meet that need. This was interpreted by the Internal Revenue Service to mean that a participant had to take out any available loans from a retirement plan first before he or she could receive a hardship distribution from the plan.

The issue with having to take out a plan loan before being able to receive a hardship distribution is that most participants who need to receive a hardship distribution are incurring adverse financial conditions. However, the amount that is available to a participant to be used for a hardship is abated by forcing the participant to take a loan from his or her account. In addition, a plan loan must be repaid. This could be difficult when a participant needs funds.

The Act remedies the financial stress that a participant may occur when he or she incurs a hardship by removing the requirement to take a loan prior to taking a hardship withdrawal.

Third, if a participant recovers from his or her hardship, the participant may wish to commence making elective deferral contributions to a plan again. However, prior to the Act, this could not be done for at least six months. This runs counter to the purpose of retirement plans which is to save for retirement. Thus, the Act removes the six-month deferral suspension requirement after a participant receives a hardship distribution.

Retirement Plan Law Changes Made by the Tax Cuts and Jobs Act

By Anthony L. Scialabba, Esq.

On December 22, 2017, President Trump signed the Tax Cuts and Jobs Act into law. A few of the provisions of the Act impact retirement plans. The following is a summary of these provisions.

I. Extended Period to Rollover Plan Loan Offset Amounts

Retirement plan loans may be offset against a participant's account for a variety of reasons. This may occur when a participant terminates employment or the plan terminates. When the loan is offset, the participant is usually taxed on the amount of the outstanding loan balance. However, a participant may avoid this result by rolling over the offset amount to an IRA or another qualified plan within 60 days.

Effective for taxable years beginning after December 31, 2017, when the loan offset is caused by termination of employment or plan termination, the period to roll over a qualified plan loan offset amount is being extended from 60 days to the individual's tax return filing due date (including extensions) for the taxable year in which the offset amount is treated as a distribution from a qualified plan.

II. Repeal of Special Rule Which Allows Recharacterization of Roth Conversions

Effective for taxable years beginning after December 31, 2017, recharacterization of a qualified rollover contribution from a non-Roth account (This includes the rollover of non-Roth contributions made to an IRA, qualified defined contribution plan, ERISA or non-ERISA 403(b) plan, or governmental section 457 plan.) to a Roth IRA is no longer permitted. Contributions made to a Roth IRA may still be recharacterized as contributions to a traditional IRA. In addition, contributions made to a traditional IRA may be recharacterized as contributions to a Roth IRA. However, only individuals who are eligible to contribute to a Roth IRA in that year may recharacterize traditional IRA contributions to Roth IRA contributions. Conversions from a traditional IRA to a Roth IRA may no longer be recharacterized at a later date following the date in which a conversion occurs. However, such conversions are still allowed.

Why Can't Part-time Employees Be Excluded From 401(k) Retirement Plans as a Class?

By Anthony L. Scialabba, Esq.[1]

Retirement plan sponsors often desire to exclude employees from being able to become eligible to participate in "tax-qualified" 401(k) retirement plans because such employees are part-time employees (including "seasonal" employees, "temporary" employees or "per diem" employees (together "Part-time Employees")). The reasons for this are such employees either do not defer salary or defer little salary into a plan. This adversely affects the nondiscrimination testing applicable to a plan. In addition, Part-time Employees often do not have a strong commitment to an employer. Thus, many employers would rather not have such employees covered under the employers' plans to save on administration costs or on the costs of having to make a "top-heavy" minimum benefit contribution to such employees. Furthermore, as the 401(k) plan industry has matured employers have increasingly wished to permit full-time employees to be able to contribute immediately without also allowing Part-time Employees to do the same. See L. Groves "IRS Attacks 401k Employee Exclusions" Zenefits Integrated HR (2018).

Although employers wish to exclude Part-time Employees from plans, many professionals who work within the retirement plan industry have wondered: "Why can't a retirement plan have a classification of excludible employees based on part-time employment status?" The argument for making such an exclusion goes: "A job classification such as clerical workers can generally be excluded, so long as the '70% ratio percentage coverage' test of section 410(b) of the Internal Revenue Code of 1986, as amended ("1986 Code"), is satisfied. So why not a job classification based on part-time employment status?" Thus, many pension practitioners wonder why any classification of employees cannot be excluded from being able to become eligible to participate in a tax-qualified retirement plan as long as the coverage tests of section 410(b) are satisfied.

This article will attempt to answer the aforementioned questions. In this regard, the history behind "tax qualification" rules of the 1986 Code that deal with participation and coverage will be examined. The rationale for not being permitted to exclude Part-time Employees will be discussed. Acceptable and unacceptable excludable classifications of employees will be set forth. Finally, suggestions will be provided for how to correct an impermissible job classification concerning Part-time Employees.

I. The History of the Ban on Excluding a Classification of Employees Based on Part-time Employment Status

A. Statutory

The history of the proscription on excluding a classification of employees based on part-time employment status begins with section 410(a) of the 1986 Code. This section of the 1986 Code provides certain minimum participation standards. In this regard, section 410(a)(1) sets forth that, in general, a plan will not be tax-qualified if the plan requires, as a condition of participation, that an employee complete a period of service with the sponsor of the plan extending beyond the later of the date on which the employee attains age 21 or the date on which he or she completes one "year of service" (or two years of service if the plan provides for full and immediate vesting upon entry into the plan) ("Year of Service/Age 21 Rule").

The origin of the Year of Service/Age 21 Rule emanates from the Revenue Act of 1942 which was signed into law by President Theodore Roosevelt on October 21, 1942 ("1942 Act"). Pub. L. 753, Ch. 619, 56 Stat. 798 (Oct. 21, 1942); see I. Bendiner, Esq. "The Revenue Act of 1942: Its Application to Life Insurance" Library of the University of Wisconsin (1942). In an attempt to statutorily define the extent to which the length of

[1] The author wishes to thank Gary S. Lesser, Esq., an author of several books with Wolters Kluwer and articles concerning retirement and executive compensation arrangements, for assisting in the research for the preparation of this article.

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service of an employee will be required to become eligible to participate in a retirement plan, the 1942 Act recognized that certain types or groups of employees should not be considered as "sufficiency employed" for "eligibility" purposes, until the employees worked in the service of the employer for a certain time period. The legislation required that a plan may exclude: 1) employees who have not been in employment for a period of five years or more, although a lesser period of eligibility may be selected by an employer; 2) employees who are employed for a period of 20 hours per week, or less; and 3) employees who are seasonal who work less than five months in a year. Id. The 1942 Act further provided that all "other" employees could be excluded, so long as the employer generally covered 70% of its employees. Id.

The participation rules set forth in the 1942 Act were later set forth in section 410(a) of the Internal Revenue Code of 1954, as amended ("1954 Code"), and in the 1986 Code. Internal Revenue Act of 1954, Pub. L. 83-591, 68A Stat. 5 (Aug. 16, 1954); Tax Reform Act of 1986, Pub. L. 99-514, 100 Stat. 2085 (Oct. 22, 1986). This section of the 1954 Code and, as mentioned above, the 1986 Code provide the Year of Service/Age 21 Rule. In addition, both Codes generally define a year of service as a 12-month period during which the employee has not less than 1,000 hours of service. See section 410(a)(3)(A) of the 1954 Code and the 1986 Code. Furthermore, both Codes provide that in the case of any seasonal industry where the customary period of employment is less than 1,000 hours during a calendar year, the term year of service shall be a period of time defined by Department of Labor regulations. See section 410(a)(3)(B) of the 1954 Code and the 1986 Code.

B. Regulatory

In an effort to clarify the One Year of Service/Age 21 Rule, the Internal Revenue Service ("IRS") published a set of proposed regulations under the authority granted to the government under section 410(a) of the 1954 Code ("Proposed Regulations"). See Preamble to Prop. Treas. Reg. § 1.410; 40 FR 45838 (Oct. 3, 1975). The Proposed Regulations acknowledge that an employer may establish conditions, other than conditions concerning age and service, that an employee be employed within a specified job classification to become eligible to participate in a tax-qualified retirement plan (and the next portion of the Proposed Regulations made reference to the "coverage" section of the 1954 Code under section 410(b) presumably in an effort to infer: "so long as the coverage rules of section 410(b) are met"). See Prop. Treas. Reg. § 1.410(a)-3(d). However, the regulations state that for purposes of applying the participation rules:

> plan provisions may be treated as imposing age or service requirements even though such provisions do not specifically refer to age or service. Plan provisions which have the effect of requiring an age or service requirement with the employer or employers maintain the plan will be treated as if they imposed an age or service requirement.

Prop. Treas. Reg. § 1.410(a)-3(e)(1).

The Proposed Regulations provide examples of how a plan provision which does not specifically refer to age or service can have the effect of requiring a service requirement. The example concerns a plan which requires one year of service as a condition of participation also excludes a part-time or seasonal employee if his or her customary employment is for not more than 20 hours per week or five months in any plan year. Prop. Treas. Reg. § 1.410(a)-3(e)(2), example (3). The regulations further state that in this example the plan would be disqualified because the provision could result in the exclusion by reason of a minimum service requirement of an employee

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who has completed a year of service. Id. In addition, the Proposed Regulations provide that the plan would not be tax-qualified even if after excluding all such employees, the plan satisfied the coverage requirements of section 410(b) of the 1954 Code. Id.

The Proposed Regulations were set forth in Final Regulations. 42 Fr 47192 (Sept. 20, 1977); T.D. 7508. The Final Regulations were essentially the same with respect to this matter, and they continued to contain the aforementioned "20 hours per week/five months" example. See Treas. Reg. § 1.410(a)-3(e)(2), example (3).

C. Other IRS Guidance

On November 22, 1994, the Employee Plans Division of the IRS issued a field directive ("1994 Field Directive") addressing the exclusion of part-time employees from participation in a tax-qualified retirement plan. The 1994 Field Directive stated that the exclusion of part-time employees (i.e., employees who work less than 40 hours per week) from a plan imposes an "indirect" service requirement on participation that could exceed one year of service. Apparently, the IRS found that the plan provisions had the "effect" of requiring an age or service requirement as referenced in the Proposed Regulations and in the Final Regulations. Thus, the 1994 Field Directive concluded that plans which exclude such employees violate section 410(a).

On November 28, 2000, the IRS issued a Technical Advice Memorandum ("TAM") that was forwarded to all EP managers. The TAM concerned the issue of whether a plan's exclusion from participation of certain employees constitutes an indirect age or service requirement in violation of section 410(a).

In its analysis of the issue, the TAM provided that the 1994 Field Directive does not apply to a consideration of a plan's indirect service requirements during its filing to obtain a Determination Letter of the tax-qualified status of the plan. The TAM further provided that the issue as to whether a plan's exclusion from participation of certain employees constitutes an indirect age or service requirement with regard to section 410(a) should be decided when the plan is examined by the IRS.

After the issuance of the TAM, specialists at the IRS involved in applications to obtain a Determination Letter that approve the tax-qualified status of a plan were instructed to include the following statement in the Determination Letter if the plan included exclusion classifications:

> A determination letter may not be relied on with respect to whether a plan's exclusion classifications, if any, violate the minimum age or service requirements of section 410 by indirectly imposing an impermissible age or service requirement.

As a result of the TAM, the IRS Publication 794 "Favorable Determination Letter" which accompanies Determination Letters issued by the government was revised in July of 2001 to include the aforementioned statement. The requirement to add the caveat at issue was omitted from the Publication when it was later revised.

On September 6, 2002, the EP Determinations "Quality Assurance Staff" ("QAS") issued guidance through a "Recurring Issue Focus" ("RIF") document addressing the acceptability of plan language that excludes from plan participation those individuals who are classified as "part-time" employees. The RIF concluded that based on the conclusion in the TAM issued November 28, 2000, specialists should not request plan administrators to remove or clarify plan language relating to part-time employees or other exclusions with indirect service related conditions because this was an audit issue, not an issue that concerned Determination Letters.

Why Can't Part-time Employees Be Excluded From 401(k) Retirement Plans as a Class?...cont'd

On February 14, 2006, the IRS issued a Quality Assurance Bulletin ("QAB") concerning Part-time Employee classifications that did three significant things. First, the QAB changed the manner in which specialists can review certain plan provisions with regard to such employees. In this regard, the QAB rescinded the RIF effective February 1, 2006. The QAB instructed IRS document examiners that they can challenge plan sponsors with plans which have potentially impermissible exclusions. Such exclusion provisions include those relating to employees based on length of service (e.g., part-time employees). In addition, the QAB instructs IRS specialists to scrutinize carefully any such exclusions to determine if they violate section 410(a). However, the QAB instructed examiners that they should not challenge an exclusion classification that is defined without reference to service (e.g., computer programmer employees).

Second, the QAB warned that improperly drafted provisions in this area could cause a plan to lose its tax-qualified status, regardless as to whether the plan was the subject of a favorable Determination Letter. The QAB stated that examiners should be aware that any exclusion classification should be closely scrutinized. In addition, the QAB encouraged specialists to require that employers clearly define any such classification.

Third, the QAB provided some suggestions for drafting plan provisions that did comply with the Year of Service/Age 21 Rule (The QAB also provided examples of provisions that were impermissible.). In one example, a plan with a one year of service initial eligibility condition defined a part-time or seasonal employee who works less than 1,000 hours of service in an eligibility computation period. The QAB stated that this plan should not be challenged. This is because the employer designed the provision at issue in such a way that there is no possibility of indirectly imposing an hour of service requirement that exceeded the maximin limit under section 410(a). The QAB stated that in the example at issue an employee that works 1,000 hours of service or more in an eligibility computation period would not meet the definition of a part-time or seasonal employee and thus would be eligible to participate in the plan.

The QAB provided another example that has more significance. This is because it provides a way for a plan to permit full-time employees to immediate enter a plan and minimize the eligibility of Part-time Employees. In this regard, the initial portion of the example set forth that a plan defines a part-time or seasonal employee as an employee who is "scheduled" to work less than 1,000 hours of service in a year. The QAB stated that in this example the plan should be challenged. The IRS noted that if the employee worked more than his scheduled hours of service he or she could conceivably be excluded even though the employee worked for over 1,000 hours of service in an eligibility computation period. However, more importantly, the QAB stated that the plan in the "scheduled" example could provide immediate eligibility for full-time employees but require one year of service for employees who are scheduled to work less than 1,000 hours of service during the computation period so long as the plan includes "fail-safe" language. This language must state that such employees will become participants if they actually work more than 1,000 during the year.

The IRS's position in the fail-safe example effectively creates two sets of eligibility conditions: one for full-time employees (immediate eligibility and participation) and one for part-time employees (one year of service eligibility). FIS Relius "Excluding Part-time, Temporary and Seasonal Employees" (2014). For example, assume that the plan in the scheduling example was a 401k plan with a calendar year plan year that contained the fail-safe provision. The plan is a top-heavy plan which provides that full-time employees are subject to immediate eligibility and entry for being able to make elective deferral contributions and receiving

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employer matching contributions. The plan provides that if a part-time employee actually works more than 1,000 hours of service during a computation period (regardless of his or her "schedule"), the employee will become a participant on the first semi-annual plan entry date following the completion of a year of service. The employer hires a full-time employee and a part-time employee on August 25, 2016. The part-time employee works 1,050 hours of service through August 24, 2017 and will become a participant on January 1, 2019.

Unlike the full-time employee in the example who will immediately be able to make elective deferral contributions, receive corresponding matching contributions and receive a top-heavy contribution for the 2016 plan year, the part-time employee in the example will not be able to defer or receive a top-heavy minimum benefit contributions during the 2017 and 2018 plan years. The part-time employee will only be able to make elective deferral contributions and receive corresponding employee matching contributions as of January 1, 2019, and the part-time employee will only be able to receive a top-heavy minimum benefit contribution for the 2019 plan year. This uneven treatment raises an issue as to whether the fail-safe exception is equitable to Part-time Employees.

It is important to note that the QAB only addresses the participation requirements of section 410(a). The QAB does not apply to the coverage rules of section 410(b). Thus, even though a fail-safe provision can exclude employees, an employer must ensure that a plan still covers a sufficient percentage of "nonhighly compensated" employees ("NHCEs" (see section 414(q) of the 1986 Code)) to satisfy these requirements.

II. Analysis

A tax-qualified retirement plan can generally exclude a classification of employees that is not based on length of service as long as the plan satisfies the minimum coverage requirements of section 410(b) of the 1986 Code (and prior to this, the 1954 Code). For example, a plan could provide that salesmen cannot be able to become eligible to participate in the plan. In general, as long as the plan in the example passed the section 401(b) coverage rules, the plan would continue to be tax-qualified. Although the plan in the example could exclude salesmen, it cannot exclude Part-time Employees, even if the plan still satisfied the coverage rules with the exclusion of the Part-time Employees. One can take the position that Part-time Employees are merely another class of employees just like salesmen. Thus, an argument can be made that the prohibition on excluding Part-time Employees is based on a distinction without merit.

Although an argument may be made that virtually any classification of employees should be able to be excluded from being able to participate in a tax-qualified plan, as mentioned above, the Final Regulations state that for purposes of applying the participation rules plan language may be treated as imposing age or service requirements without specifically referring to them. In addition, plan language that has the effect of requiring an age or service requirement with the employer or employers maintain the plan will be treated as if they imposed such a requirement. Furthermore, in the example cited in the regulations, the IRS provides that the plan would not be tax-qualified even if after excluding all such employees, the plan satisfied the coverage requirements of section 410(b). Therefore, an exclusion of a classification of employees based on length of service will generally not be accepted by the government.

The rationale for the IRS's position regarding "length of service" exclusions is probably due to the fact that section 410(a) already provides employers with a way to exclude employees based on length of service. See M. Clee "A Trap for the Unwary Employer: Failure to Cover Part-time and Temporary Employees Under a 401(k) Plan" Fenwick & West LLP (2009). An

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employer can decide to avail itself to the exclusion in this section that "caps out" at 1,000 hours of service in a year. Id. However, if an employer chooses not to utilize the statutory exclusion, it should not be able to subvert the rules by implementing into a plan a job classification exclusion based on service. Id. Thus, to summarize, the position of the IRS is that Part-time Employees may not be excluded as a class because section 410(a) already "speaks" to the issue.

III. Employee Job Classification Exclusions that Are and Are not Permitted

The exclusions that are permitted are ones that are not based on length of service. Thus, agricultural workers, custodians, and interns would be acceptable. Even job classifications that "concern" time, but not a "length of time" would be upheld. These categories include hourly employees, shift workers and night watchmen. In addition, part-time employees subject to the fail-safe provision discussed above would be acceptable. Furthermore, even some definitions based on length of time will be upheld. For example, a plan excludes part-time employees, and a part-time employee is defined as an employee who has not yet completed a year of service (1,000 hours of service in a year) would be acceptable.

The job classifications exclusions that would not be permitted are ones that are based on length of service either directly or indirectly. Examples of job classifications that would not be allowed are obviously part-time employees (or part-time employees whose customary employment schedules are less than 20 hours or fewer a week) and seasonal employees like summer associates at a law firm. An impermissible exclusion would also include per diem workers even though they are paid for one day's work. This is because either part-time employees, seasonal employees or per diem employees could conceivably work over 1,000 hours of service in a year. However, as mentioned above, the class exclusion cannot indirectly be based on length of service. Thus, for example, if a plan excluded warehouse workers and they are all part-time employees, this would effectively exclude part-time employees by attempting to disguise them as a proper classification.

IV. What an Employer Should Do if the Rules Are Violated

A. Why Violations of the Rules Occur

One reason for why the Year of Service/Age 21 Rule is violated is because employers often falsely believe that they are permitted to exclude Part-time Employees so long as the classification of employees that is excluded does not cause the 70% ratio percentage coverage test of section 410(b) to be failed.

Another reason for why the rule at issue is breached concerns employer-sponsored health care and welfare plans. Such plans often require that Part-time Employees be excluded. In fact, an employer who does not preclude such employees from coverage may have adverse consequences with the employer's insurance carrier. See M. Clee "A Trap for the Unwary Employer: Failure to Cover Part-time and Temporary Employees Under a 401(k) Plan" Fenwick & West LLP (2009). Thus, an employer that must exclude Part-time Employees from its health and welfare plan may believe that the employer can exclude such employees from its 401k plan. See id.

B. IRS Programs Available to Resolve Plan Defects

Employers should scrutinize the manner in which their retirement plans are operated and documents are drafted to determine whether an exclusion of a job classification of employees violates the Year of Service/Age 21 Rule. When an employer detects that a violation of this rule has occurred, the employer may resolve this defect through the utilization of the IRS's "Employee Plans Compliance Resolution System" ("EPCRS"). Rev. Proc. 2016-51. Essentially, this is a

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retirement plan "fix-it" program that is available for resolving tax qualification defects.

The "Self-correction Program" ("SCP") is one way to resolve a tax qualification defect in a retirement plan under EPCRS. Rev. Proc. 2016-51, Part IV. This program applies to defects that are "operational" in nature. Under SCP, a plan sponsor can correct a "significant" defect that occurred within two plan years before the plan year in which the correction is made. However, if the defect is "insignificant", then a plan sponsor can generally correct the defect no matter when it occurred. Thus, SCP can be utilized to correct a defect when a plan is operated in a manner which excludes Part-time Employees.

If employees are mistakenly excluded from a plan, SCP requires an employer to make certain contributions on behalf of the "affected" employees. SCP provides rules that apply to each type of contribution at issue (employee and/or employer). In this regard, if an affected employee is properly enrolled in a plan no later than three months following the initial failure, then no corrective contribution is required for the missed deferral opportunity. However, matching contributions (if applicable), including earnings accrued thereon, are required to be made to the plan. In addition, a notice must be sent to the affected employees that details the facts that concern why the contribution is being made.

If the failure is discovered beyond three months but less than two years (the end of the self-correction period) after the failure, SCP requires that a "qualified nonelective" contribution will be required to be made to the affected employee to compensate him or her for the "missed deferral" opportunity. Matching contributions (if applicable), earnings accrued on the corrective contributions and a notice to affected participants are also required.

The "Voluntary Correction Program" ("VCP") is another way in which defects can be corrected in EPCRS. Rev. Proc. 2016-51, Part V. This program requires a formal submission to the IRS. In addition, VCP applies to "document" defects. Thus, if a plan contains a class exclusion that violates the Year of Service/Age 21 Rule, the plan can be corrected in VCP though the utilization of a retroactive amendment to either remove the impermissible classification or to revise it to one that is acceptable. In addition, corrective contributions would have to made to all employees who were incorrectly excluded because of the impermissible classification. VCP also requires the payment of a relatively small "user" fee to the IRS.

V. Conclusion

To answer the questions posed in the introduction to this article, an exclusion of an employee job classification from a tax-qualified retirement plan based on length of service will cause a violation of the Year of Service/Age 21 Rule. This occurs regardless as to whether a plan satisfies the 70% coverage test of the Code when the exclusion is made. This is why Part-time Employees may not be excluded from a retirement plan as a class. However, with creative plan drafting, the impact of the rule can be minimized to some degree.

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